

**ECONOMIC REFERENCES COMMITTEE OF THE SENATE
AUSTRALIAN PARLIAMENT – 19 FEBRUARY 2014**

**An inquiry into the performance of the Australian
Securities and Investments Commission (ASIC).**

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ASIC's Performance Must be Supported by Appropriate Powers

It is appropriate to judge ASIC's performance only on the powers it actually has;

There are a number of misconceptions about what ASIC can do which do not match up with its powers: ASIC is an enforcement not prudential regulator; ASIC has limited powers to obtain compensation for consumers; until recently it was difficult for ASIC to cancel Australian Financial Services Licenses and to ban individuals;

ASIC's powers rely too much on disclosure in regulating for financial consumers;

The Wallis Committee settings were not directed particularly to financial consumers and were before much of the financial consumer capability research;

ASIC needs supplementary powers, which go to the suitability and fairness of some products for financial consumers. For example powers to require product modifications or powers to prohibit. It would be fairer to reset the market expectations from caveat emptor to caveat vendor;

We should consider whether the objects and purposes that have been set for ASIC in the ASIC Act need reconsideration: is it appropriate in a country with compulsory superannuation to speak of 'investor confidence' (related to disclosure and investment choice) or should we be thinking about 'investor protection' when we now know many people do not have the capabilities to make good investment decisions?

ASIC needs fine-tuning of some of its existing powers: for example telecommunications interception warrants, search warrant powers, its powers to bring civil penalty proceedings. ASIC has been given many new legislative mandates over its span and there could be some rationalisation so that where possible powers under these mandates are identical or harmonised; recalibrating the definition of 'retail client' and 'sophisticated investor' is also a priority;

Some of ASIC's powers were set in 1989 on its creation. Universal superannuation coverage did not come in until 1992. ASIC's powers which have grown in many different directions since, need to be adjusted to the 'mass market' nature of financial services provision in a country where every employee will be an investor: enforceable undertakings and infringement notices are a start, but we need to improve these and think of other ways to address the 'democratisation of finance'.

Regulatory Design is Important to ASIC's Performance

Badly designed or out of date regulation lets down the regulator, the regulated and the beneficiaries of regulation. Since the purpose of financial and corporate transactions is the growth of the real economy and the welfare of Australians, poor regulatory design affects everyone;

It is important not to spend resources regulating apparent innovations which do not benefit the real economy: good regulatory design might require a regulator to use prohibition of certain products or services which might benefit financial intermediaries but provide little other benefit;

We have suggested the use of 'self-executing' provisions. For example we think all Financial Services Licensees should be public companies, with an obligation to make their audited financial statements publically available. Likewise we suggested that all financial services licensees should have to provide annual board certification of compliance with license conditions and financial services laws. If this certification is late it could lead to automatic license suspension. If it is later than 3 months the entity should have its licence withdrawn.

Good regulatory design would also bring the corporate nature of a licensee into line with the regulatory obligations of its personnel. So for example, if a person were banned from acting as an advisor, they should also be disqualified from being a director or officer of a licensee and dispose of shares if they are a majority shareholder;

Better protecting whistle-blowers, expanding the matters they can report and introducing whistle-blower 'bounties' as in the qui-tam suits in the US are all examples of better regulatory design;

Clarifying the purposes of criminal and civil penalty provisions and how and when they should be used, would also improve regulatory design;

In the retail investor area it would also improve the performance of ASIC if there were an investor compensation scheme. At the moment a significant value of orders in favour of clients by dispute resolution bodies are not met, often because the licensee is insolvent.

Finally, ASIC's role would be more effective if the design of regulation made its morals and ethics – its normative impact - clearer. This is important because for providers to comply they have to believe in the ethics conveyed by the regulation they are complying with. A topical example is the banning of conflicted

remuneration. A ban sends a clear message about the quality of financial advice required: no conflicts, put the client first. A ban is ethically straightforward and should be easy to train representatives to hold as a personal value, and translate into the culture of a financial organisation. Adopting such a clear position, might let you discard a complex 'best interests' duty - for if you have banned conflicted remuneration there is much less for the 'best interests' duty to act on. A complex 'best interests' duty is much more ambiguous ethically and provides less clear guidance to those subject to it. ASIC will be more effective if those subject to the regulation it administers not only understand, but accept as right the morals and ethics of the regulation ASIC administers. Normative clarity as part of regulatory design will help that.

Absolutely finally, good design goes not only to regulation of the population of financial providers. It is also relevant to the governance of the regulator and its relationship with the Minister and Department. We think that ASIC and the Minister should exchange annually, a Statement of Intention from ASIC of how, what and why it will regulate, and a Statement of Expectations from the Minister to ASIC as to regulatory priorities within ASIC's legislative mandate. The exchange should include real regulatory priorities with implementation detail: it should not be a general and vague wish list. This dialogue occurs anyway, and we think there is much to be said for formalising the discussion in a written exchange and making it public.